Ciech

Santander Biuro Maklerskie

Bloomberg: CIE PW Reuters: CIE.WA

CEE Equity Research

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Threats on macro-side in the short run

Recommendation Neutral. TP set at PLN53.4

We are setting Dec'24 TP for Ciech at PLN53.4, which results in a Neutral recommendation for the stock. Recent months have flourished primarily when it comes to corporate events, which finally resulted in a hefty dividend pay-out and KI Chemistry stake increase to almost 78%. From the business perspective, we reckon the market environment got even more challenging, negatively affecting the mid-run financial outlook (soda ash and agro divisions appear the most exposed to deteriorated trends). Optimistic is the fact that Ciech's MB remains self-confident and guides FY23E EBITDA in the range of PLN860-920mn. This, in turn, allows for some optimism regarding the potential for FCF yield delivery. FY23E comparative valuation metrics (FY23E P/E at 10.9x and EV/EBTIDA at 5.1x) appear still not particularly demanding, but may offer limited space for rerating, taking into account the current stage of the economic cycle.

Recent developments. Recent months have flourished primarily when it comes to corporate events. As a result, KI Chemistry increased its stake in the company to almost 78% voting rights EOP 1H23E. In the meantime, the AGM voted for regular dividend pay-out in the amount of PLN5.75mn/sh (to be finally paid out on July 17^{th}). Regarding the business trends, Ciech continues to struggle with decreasing sales volumes in its key soda ash segment (-20% y/y in 1Q23) and others. The negative y/y volume effect is associated with (1) lower GDP output (PUR foams segment), (2) high product stocks held by distributors (agro division) and (3) downturn in the EU construction industry (particularly negatively affecting the soda ash segment). At this point, we emphasize the risk that the unsupportive business conditions could last longer and could result in further y/y volume decrease in the mid-run (already evidenced in 2Q23E).

Vague mid-run business outlook... We associate the key short-/mid-run risks with the increasing competitive pressure resulting from the slowing economy. Above all, from the strategic point of view, the expected gradual increase in soda ash capacity worldwide (China, Turkey and the USA) in coming years, which in turn may translate into even greater intensification of pressure on product prices.

...Does not undermine MB's self-confidence. Official Ciech's FY23 guidance (dated end of May 2023) points to consolidated revenues in the range of PLN5.95bn-PLN6.35bn and EBITDA close to PLN860mn-PLN920mn. Having contrasted these assumptions with the current stage of the economic cycle and more challenging business environment (related also to potentially inflated energy costs), we interpret the goals as ambitious but achievable.

Attractive FCF profile. Ciech expects its FY23 capex to settle between PLN 500 – 600mn. The lion's share of the capital outlays is devoted to development initiatives. Having paired this with the company's priorities such as drive for (1) operational excellence, (2) optimization of technological processes, (3) energy transformation and (4) decarburization as well as development of the product portfolio, we believe the company is on the track to become a highly optimized multi-segment organization capable of regular robust financial performance delivery.

Opportunities & risks. The depth and time of the economic downturn, feedstock availability, demand for products, and ability to swiftly monetize the capex are among the key business risks. We point out also the potentially unfavorable tendencies in terms of labour, external services and energy costs. On top, price tendencies of CO_2 emission allowances also generate considerable risks to our valuation.

Valuation. The DCF model points to PLN46.7 per share (a 6% downside). The comparative valuation implies fair value at PLN73.6 /sh. Adopting a mixed approach (DCF: 75%; CV: 25%), we arrive at TP of PLN53.4 (7% upside potential). In effect, we issue a Neutral rating for the stock.

Financial summary

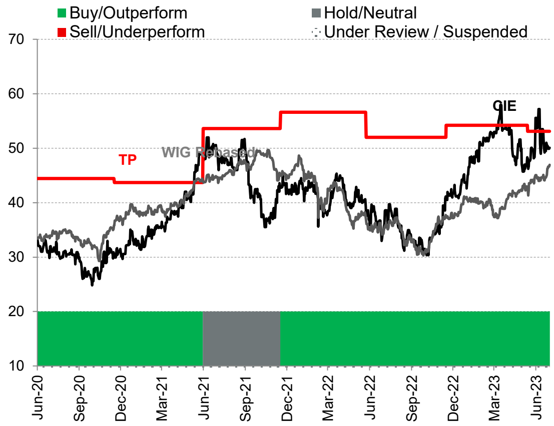
PLNmn	2020	2021	2022	2023E	2024E	2025E
Revenues	2,976	3,460	5,415	5,836	5,655	5,672
EBITDA	589	730	989	816	961	1,019
EBIT	250	356	590	365	502	554
Net profit	123	230	563	240	363	411
P/E (x)	13.5	11.4	4.7	10.9	7.2	6.4
EV/EBITDA (x)	5.6	5.3	4.0	5.1	4.1	3.7
FCF Yld	-4.0%	13.0%	-0.6%	6.5%	12.0%	13.9%
DY	0.0%	6.0%	3.0%	11.5%	2.8%	4.1%

Source: Company data, Santander Brokerage Poland estimates

Recommendation	Neutral
Target Price (PLN, Dec'24)	53.4
Price (PLN, 14 July 2023)	49.9
Market cap. (PLNmn)	2,630
Free float (%)	22.3
Number of shares (mn)	52.7

What has changed

- More cautious volumes assumption in soda ash and agro segment;
- Slightly lower assumptions regarding operational margins across all the business segment in the short run;
- Dividend-pay-out ratio updated following recent regular dividend payment approval by AGM.



The chart measures performance against the WIG index.

Main shareholders	% of votes
KI Chemistry S.a r.l	77.7
NN PTE S.A.	7.18

Source: gpw.pl

Analyst

Michał Sopiel, *Equity Analyst*

+48 22 586 82 33 michal.sopiel@santander.pl

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Forecasts & Valuations

DCF valuation

Fig. 1. WACC calculation*

Risk-free rate	5.0%
Unlevered beta	1.0
Levered beta	6.0%
Equity risk premium	1.3
Cost of equity	**12.9%**
Risk-free rate	5.0%
Debt risk premium	1.1%
Tax rate	23.0%
After tax cost of debt	**4.7%**
%D	30.0%
%E	70.0%
WACC	**10.4%**

*Source: Santander Brokerage Poland estimates, *in the terminal period*

Fig. 2. Forecast changes

PLNmn	2023E			2024E			2025E		
	New	Previous	Change	New	Previous	Change	New	Previous	Change
Revenues	5,836	5,340	*9%*	5,655	5,355	*6%*	5,672	5,287	*7%*
EBITDA	816	905	*-10%*	961	951	*1%*	1,019	980	*4%*
EBIT	365	454	*-20%*	502	493	*2%*	554	515	*8%*
Net profit	240	309	*-22%*	363	343	*6%*	411	365	*13%*

Source: Santander Brokerage Poland estimates

Fig. 3. DCF valuation

DCF valuation (PLN mn)	2023E	2024E	2025E	2026E	2027E	>2027E
EBIT	**364.6**	**502.4**	**554.2**	**556.4**	**559.0**	**491.7**
Tax rate	19%	19%	19%	19%	19%	19%
Taxes on EBIT	69.3	95.5	105.3	105.7	106.2	93.4
NOPLAT	**295.3**	**407.0**	**448.9**	**450.7**	**452.8**	**398.3**
Depreciation	451.8	458.6	465.2	471.4	477.2	477.2
Capital expenditures	551.4	551.4	551.4	551.4	551.4	477.2
Change in working capital	-62.6	-29.6	-3.1	-4.2	-1.1	0.0
Free cash flow	**133.1**	**284.7**	**359.5**	**366.5**	**377.5**	**398.3**
WACC	11.1%	11.2%	11.3%	10.4%	10.5%	10.4%
Enterprise value	**3,351**					
Net debt at EOP 2022	1,212					
Minorities	5.9					
Dividend paid	5.75					
Fair value EOP 2022	**1,842**					
Number of shares	52.7					
Fair value per share EOP 2022	**35.0**					
Target Price (Dec'24)	**46.7**					

Source: Santander Brokerage Poland estimates

Comparative valuation

Fig. 4. Comparative valuation

Company	Price	Curr	Market Cap (EURm)	P/E 2023E	P/E 2024E	P/E 2025E	EV/EBITDA 2023E	EV/EBITDA 2024E	EV/EBITDA 2025E
Ciech	**49.9**	**PLN**	**590**	**10.9**	**7.2**	**6.4**	**4.7**	**4.0**	**3.8**
BASF SE	46.43	EUR	41,502	11.3	9.4	8.2	7.1	6.1	5.5
Bayer AG	50.63	EUR	49,740	7.1	6.7	6.2	6.9	6.5	6.2
Solvay SA	105.4	EUR	11,159	7.8	7.9	7.3	5.0	5.0	4.7
Tata Chemicals Ltd	977	INR	2,708	10.7	10.7	12.4	7.5	7.5	8.1
LANXESS AG	29.86	EUR	2,578	17.4	9.0	6.7	9.4	7.1	6.2
Grupa Azoty SA	28.32	PLN	632	n.a.	n.a.	n.a.	12.6	8.3	5.3
Median				10.7	9.0	7.3	7.3	6.8	5.9
Premium/discount vs. median				2%	-19%	-12%	-35%	-41%	-36%

Source: Santander Brokerage Poland estimates, Bloomberg

Fig. 5. Implied share prices vs. peers valuation (PLN)

	P/E 2023E-25E	EV/EBITDA 2023E-25E	Average
Per share value	55.8	91.4	**73.6**

Source: Santander Brokerage Poland estimates

Fig. 6. per share valuation (PLN)

	New	Previous	Change
DCF valuation	46.7	45.0	*4%*
Comparable valuation (based on 2023-25E)	73.6	77.3	*-5%*
Weighted average*	**53.4**	**53.1**	***1%***

*Source: Santander Brokerage Poland estimates, *DCF: 75%; CV: 25%. Higher weight has been assigned to DCF as a prime valuation tool relying on the long-term outlook.*

Based on our DCF-model derived valuation pointing at PLN46.7 per share (a 75% weight) and comparative valuation indicating PLN73.6 value per share (a 25% weight), we set a TP at PLN53.4.

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Fig. 7. Income statement forecasts

PLNmn	2018	2019	2020	2021	2022	2023E	2024E	2025E
Net sales	**3,673**	**3,549**	**2,976**	**3,460**	**5,415**	**5,836**	**5,655**	**5,672**
COGS	-2,909	-2,767	-2,345	-2,812	-4,247	-4,807	-4,483	-4,427
Gross profit	**763**	**782**	**631**	**648**	**1,168**	**1,029**	**1,172**	**1,244**
SG&A	-417	-453	-344	-472	-590	-686	-700	-721
Other operating income, net	33	-61	-37	181	12	21	30	30
EBITDA	**654**	**578**	**589**	**730**	**989**	**816**	**961**	**1,019**
Operating profit	**379**	**268**	**250**	**356**	**590**	**365**	**502**	**554**
Net financial income (costs)	-69	-87	-62	-84	0	-85	-54	-47
Profit before tax	**311**	**180**	**188**	**272**	**590**	**280**	**448**	**507**
Income tax	128	67	65	42	27	40	85	96
Net profit after minorities	**183**	**113**	**123**	**230**	**563**	**240**	**363**	**411**
Gross margin	20.8%	22.0%	21.2%	18.7%	21.6%	17.6%	20.7%	21.9%
EBITDA margin	17.8%	16.3%	19.8%	21.1%	18.3%	14.0%	17.0%	18.0%
Operating margin	10.3%	7.5%	8.4%	10.3%	10.9%	6.2%	8.9%	9.8%
Net profit margin	5.0%	3.2%	4.1%	6.6%	10.4%	4.1%	6.4%	7.2%

Source: Company data, Santander Brokerage Poland estimates

Fig. 8. Balance sheet forecasts

PLNmn	2018	2019	2020	2021	2022	2023E	2024E	2025E
Current assets	**1,273**	**1,312**	**1,456**	**2,348**	**3,192**	**3,363**	**3,222**	**3,221**
Fixed assets	**3,559**	**3,734**	**4,251**	**4,798**	**4,901**	**4,953**	**5,043**	**5,130**
Total assets	**4,831**	**5,046**	**5,708**	**7,146**	**8,093**	**8,316**	**8,265**	**8,351**
Current liabilities	**1,234**	**1,122**	**3,188**	**2,207**	**3,207**	**3,252**	**3,098**	**3,067**
bank debt	298	90	1,937	35	224	255	231	208
Long-term liabilities	**1,628**	**1,947**	**401**	**2,542**	**2,181**	**2,421**	**2,234**	**2,048**
bank debt	1,358	1,700	104	1,975	1,776	2,016	1,828	1,643
Equity	**1,970**	**1,978**	**2,121**	**2,401**	**2,710**	**2,648**	**2,939**	**3,241**
share capital	288	288	288	288	288	288	288	288
Minority Interest	**0**	**-1**	**-2**	**-4**	**-6**	**-6**	**-6**	**-6**
Total liabilities	**4,831**	**5,046**	**5,708**	**7,146**	**8,093**	**8,316**	**8,265**	**8,351**
Net debt	1,464	1,490	1,597	1,212	1,315	1,532	1,344	1,133

Source: Company data, Santander Brokerage Poland estimates

Fig. 9. Cash flow statement forecasts

PLNmn	2018	2019	2020	2021	2022	2023E	2024E	2025E
CF from operations	**454**	**532**	**767**	**1,284**	**614**	**721**	**866**	**918**
CF from investment	**-627**	**-407**	**-834**	**-707**	**-629**	**-551**	**-551**	**-551**
CF from financing	**-125**	**-17**	**212**	**-222**	**-99**	**-118**	**-338**	**-365**
dividends paid	-395	0	0	-158	-79	-303	-72	-109
Net change in cash	**-298**	**107**	**144**	**355**	**-114**	**52**	**-23**	**2**

Source: Company data, Santander Brokerage Poland estimates

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Santander Brokerage Poland

Jana Pawla II Avenue 17
00-854 Warszawa
fax. (+48) 22 586 81 09

Equity Research

Kamil Stolarski, PhD, CFA, *Head of Equity Research* *Banks, Insurers, Strategy*	tel. (+48) 22 586 81 00	kamil.stolarski@santander.pl
Paweł Puchalski, CFA, *Equity Analyst* *Telecommunications, Metals & Mining, Power*	tel. (+48) 22 586 80 95	pawel.puchalski@santander.pl
Tomasz Krukowski, CFA, *Equity Analyst* *Oil&Gas, Pharma & Biotech, CEE Non-Financials*	tel. (+48) 22 586 81 55	tomasz.krukowski@santander.pl
Adrian Kyrcz, *Equity Analyst* *Construction, Real Estate, IT*	tel. (+48) 22 586 81 59	adrian.kyrcz@santander.pl
Tomasz Sokołowski, *Equity Analyst* *Consumer, E-commerce*	tel. (+48) 22 586 82 36	tomasz.sokolowski@santander.pl
Michał Sopiel, *Equity Analyst* *Industrials, Chemicals, Quantitative Analysis*	tel. (+48) 22 586 82 33	michal.sopiel@santander.pl
Piotr Zielonka, CFA, *Equity Analyst* *Gaming, Strategy*	tel. (+48) 22 534 16 10	piotr.zielonka@santander.pl
Marcin Działek, *Analyst* *Technical Analysis*	tel. (+48) 22 782 93 09	marcin.dzialek@santander.pl

Sales & Trading

Kamil Kalemba, *Head of Institutional Equities*	tel. (+48) 22 586 80 84	kamil.kalemba@santander.pl
Mateusz Choromański, CFA, Head of Sales *Securities Broker, Investment Advisor*	tel. (+48) 22 586 80 82	mateusz.choromanski@santander.pl
Alex Kamiński	tel. (+48) 22 586 80 63	alex.kaminski@santander.pl
Błażej Leśków, *Securities Broker*	tel. (+48) 22 586 80 83	blazej.leskow@santander.pl
Michał Stępkowski, *Securities Broker*	tel. (+48) 22 586 85 15	michal.stepkowski@santander.pl
Marek Wardzyński, *Securities Broker*	tel. (+48) 22 586 80 87	marek.wardzynski@santander.pl
Adam Mizera, *ACCA, CFA, Securities Broker*	tel. (+48) 22 586 85 14	adam.mizera@santander.pl

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In preparing this report Santander Brokerage Poland applied at least one of the following valuation methods: discounted cash flows (DCF), comparative, mid-cycle, dividend discount model (DDM), residual income, warranted equity method (WEV), SOTP valuation, liquidation value.
The discounted cash flows (DCF) valuation method is based on expected future discounted cash flows. One advantage of the DCF valuation method is that it takes into account all cash streams reaching Issuer and the cost of money over time. Some disadvantages of the DCF valuation method are that a large number of parameters and assumptions need to be estimated; and the valuation is sensitive to changes in those parameters.
The comparative valuation method is based on the economic rule of "one price". Some advantages of the comparative valuation method are that the analyst need only estimate a small number of parameters; the valuation is based on current market conditions; the relatively large accessibility of indicators for companies being compared; and that there is an extensive knowledge of the comparative method among investors. Some disadvantages of valuation by the comparative method are the considerable sensitivity of the results of the valuation on the choice of companies to the comparative group; the method can lead to a simplification of the picture of the company which in turn can lead to omitting certain important factors (e.g. growth dynamics, extra-operational assets, corporate governance, the repeatability of results, differences in applied accounting standards); and the uncertainty of the effectiveness of a market valuation of companies being compared.
The mid-cycle multiple valuation is based on long-term average valuation multiples of a sector or a peer group. The methodology aims to calculate a fair, through the cycle value of the company. Among its shortfalls is that at peaks and/or troughs of the cycle, the implied fair value may deviate substantially from the market's value of an analysed stock as well as the methods' reliance on the quality of external data (we usually use Bloomberg or Damodaran databases). Simplicity and average through-cycle value allowing to capture over- as well as under-valuation of a given stock are the main advantages of this methodology.
The dividend discount model (DDM) valuation is based on the net present value of the future dividends that are expected to be paid out by the company. Some advantages of the DDM valuation method are that it takes into account real cash flows to equity-owners and that the methodology is used in respect to companies with long dividend payout history. Main disadvantage of the DDM valuation method is that dividend payouts are based on a large number of parameters and assumptions, including dividend payout ratio.
Residual income method is conceptually close to the discounted cash flows method (DCF) for non-financial stocks, the difference being that it is based on expected residual income (returns over COE) rather than expected future cash flows. One advantage of this valuation method is that it captures the excess of profit potentially available to shareholders and the cost of money over time. Main disadvantage of the valuation method is that a large number of parameters and assumptions need to be estimated; and the valuation is sensitive to changes in those parameters.
The warranted equity method (WEV) is based on the formula P/BV = (two year forward ROE less sustainable growth rate)/(Cost of equity less sustainable growth rate) which allows estimating a fair value (FV) of a given stock in two years' time. Subsequently the FV is discounted back to today. The main advantage of the WEV method is that it is a transparent one and based on relatively short term forecasts, hence substantially reducing the margin of forecasting error. The main disadvantage in our view is that the model is based on the principle that stock price should converge towards its fair value implied by company's ROE and COE.
SOTP valuation - different assets of a company are being valued according to different valuation methods, and the sum of these valuations represents the final valuation of the company. SOTP valuation advantages / disadvantages are identical to advantages and disadvantages of the specific valuation methods used.
Liquidation value method – liquidation value is the estimated amount of money that an asset or company could be quickly sold for, such as if it were to go out of business. Then, the estimated assets value is adjusted for liabilities and liquidation expenses. One advantage of this valuation method is its simplicity. This method does not account for intangible assets as goodwill, which is the main disadvantage.

In the opinion of Santander Brokerage Poland, this report has been prepared with all due diligence and excludes any conflict of interests which could influence its content.
In Santander Bank Polska there are implemented internal regulations, which are designed to prevent conflicts of interest concerning recommendations. Physical and logic barriers are established, and the principles of documentation adequate to the type of Santander Bank Polska operations are implemented. Additionally, Santander Bank Polska introduced a number of obligations and restrictions relating to the protection of confidential information flow between organizational units.
The date and time on the first page of this report indicates the date of the production of the recommendation, and the dissemination of the recommendation takes place on the same day before the start of the session.

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